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**Internal Revenue Service**

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Date:  
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**LEGEND:**

Distributing =

Controlled =

Distributing Common Stock =

Controlled Common Stock =

Business 1 =

Business 2 =

Controlled Note =

LLC 1 =

State L =

Shareholder A =

Shareholder B =

Shareholder C =

Shareholder D =

Shareholder E =

Date A =

Date B =

Date C =

Date D =

a =

b =

c =

d =

W =

X =

Y =

Z =

Dear :

This letter responds to your letter dated March 30, 2006, requesting rulings as to the federal income tax consequences of a proposed transaction. Additional information was submitted on June 23, 2006, July 21, 2006, July 27, 2006 and August 9, 2006. The information submitted is summarized below.

The rulings contained in this letter are based on facts and representations submitted by the taxpayer and accompanied by a penalty of perjury statement executed by an appropriate party. This office has not verified any of the materials submitted in support of the request for rulings. Verification of the information, representations, and other data may be required as part of the audit process. Moreover, no information provided by the taxpayer has been reviewed and no determination has been made regarding whether the proposed transaction: (i) satisfies the business purpose requirement of § 1.355-2(b) of the Income Tax Regulations; (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see § 355(a)(1)(B) of the Internal Revenue Code (the "Code") and § 1.355-2(d)) or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a fifty percent or greater interest in the distributing corporation or the controlled corporation (see §§ 355(e)(2)(A)(ii) and 1.355-7).

#### SUMMARY OF FACTS

Distributing is an accrual basis State L corporation and the common parent of an affiliated group of corporations that files a consolidated federal income tax return. Distributing has a single class of voting common stock outstanding, which is widely held and publicly traded. Each share of Distributing Common Stock also evidences one preferred share purchase right to purchase Distributing Common Stock on the occurrence of certain events involving a change in control of Distributing (the "Distributing Purchase Rights"). Shareholders A, B, C, D, and E each own more than five percent of Distributing Common Stock (the "Institutional Investors"). Other than Shareholder E, no Institutional Investor has a representative on Distributing's board of directors.

Controlled has a single class of voting common stock outstanding. Each share of Controlled Common Stock evidences a purchase right similar to the Distributing Purchase Rights (the "Controlled Purchase Rights"). Prior to Date A, Distributing owned all of the outstanding stock of Controlled.

Distributing conducts Business 1. Controlled presently conducts Business 2 through LLC 1, a State L limited liability company that is wholly owned by Controlled and is disregarded for federal income tax purposes. Financial information has been received indicating that each of Business 1 and Business 2 has had gross receipts and operating expenses representative of an active trade or business for each of the past 5 years.

Business 1 and Business 2 have increasingly competed for the same customers. In order to resolve the conflicts that have arisen as a result of the operation of both businesses in the same affiliated group, Distributing plans to distribute all of the issued and outstanding shares of Controlled Common Stock beneficially owned by Distributing to holders, as of the record date, of the issued and outstanding shares of Distributing Common Stock (the "Distribution"), which is intended to improve the business prospects of both businesses.

Depending on market conditions, Distributing may purchase up to W percent (an amount greater than twenty percent) of its outstanding shares after the Distribution. Such purchases will be through either open market purchases, block purchases, accelerated share repurchase transactions, a Modified Dutch Auction tender offer, or some combination thereof.

For instance, in order to facilitate large stock purchases and to enhance the effectiveness of its stock purchasing program, Distributing may purchase its shares from an investment or commercial bank ("Broker/Bank") pursuant to an accelerated share repurchase program ("ASR"). In an ASR, Distributing purchases a specified number of its common shares from Broker/Bank and pays to Broker/Bank an estimated price per share (the "Initial Price"), which is equal to the average price of Distributing Common Stock on the previous day. Broker/Bank obtains the shares delivered to Distributing by "borrowing" shares of Distributing Common Stock from the stock market. In the subsequent weeks, the Broker/Bank buys shares on the open market in an amount equal to the number of borrowed shares and returns the shares it borrowed to the initial stock lenders.

Once the purchase program is completed, Distributing and Broker/Bank "true-up" to take into account any difference between the Initial Price when Distributing purchased the shares and the average price Broker/Bank paid for the shares over the subsequent weeks. To help minimize the exposure to market price fluctuations on the "true-up" price, Distributing may enter into an agreement with the Broker/Bank to establish a minimum and maximum price Distributing is willing to pay for its share repurchases. Under such an agreement, the "true-up" cannot exceed certain parameters.

Distributing may also purchase shares through block purchases allowed under Rule 10b-18 of the Securities Exchange Act of 1934. Such purchases may be privately negotiated purchases, either directly or through Distributing's broker. While the identity of the seller may be known to Distributing or its broker, all such sales will occur in compliance with the provisions of Rule 10b-18. Distributing will not make any block purchases of shares from any Institutional Investor or any shareholder who owns five percent or more of the stock in, or the securities of, Distributing at the time of the purchase.

Depending on market conditions, Controlled may purchase up to X percent (an amount that is not greater than twenty percent) of its outstanding shares after the Distribution through open market purchases (the "Controlled Repurchases").

## PROPOSED TRANSACTION

In accordance with the Distribution, the following transaction has been proposed and partially consummated:

- (i) Prior to Date A, Controlled distributed the Controlled Note to Distributing. On Date B, a foreign subsidiary of Controlled borrowed a from its credit facilities and distributed the proceeds to Controlled. On Date C, Controlled used the proceeds from such borrowings to pay b in principal and c in interest on the Controlled Note. Using the net proceeds from the initial public offering of its common stock, described in step (iii), below, and available cash, Controlled fully paid the balance of the Controlled Note on Date D.
- (ii) Prior to Date A, intercompany notes and accounts receivable from Controlled, exclusive of the Controlled Note, were set off against intercompany notes and accounts payable to Controlled with d of net notes and accounts receivable being distributed as a dividend in kind from Controlled to Distributing.
- (iii) On Date A, Controlled issued Y shares of Controlled Common Stock to the public in an initial public offering. As a result of this offering, Distributing's percentage ownership of the Controlled Common Stock decreased to Z percent.
- (iv) Distributing will distribute all of the issued and outstanding shares of Controlled Common Stock beneficially owned by Distributing, which will represent a number greater than eighty percent of the outstanding shares of the Controlled Common Stock, to holders, as of the record date, of the issued and outstanding shares of Distributing Common Stock. The Distribution will be by means of a dividend of Controlled Common Stock to Distributing's shareholders on a pro rata basis. No holder of Distributing Common Stock will be required to pay any cash or any other consideration for the shares of Controlled Common Stock to be received in the Distribution or to surrender or change shares of Distributing Common Stock in order to receive shares of Controlled Common Stock. Distributing shareholders will receive cash in lieu of fractional shares in the Distribution.

Distributing and Controlled have recently entered into a series of agreements governing the Distribution and the relationships between Distributing and Controlled subsequent to

the Distribution, including the provision of services and providing for the allocation of tax and certain other liabilities and obligations arising from periods prior to the Distribution (collectively, the "Separation Agreements"). Distributing and Controlled will have certain other continuing relationships following the Distribution, all of which will be based on terms and conditions arrived at by the parties bargaining at arms' length.

## REPRESENTATIONS

The following representations have been made with respect to the Distribution:

- (a) No part of the Controlled Common Stock to be distributed by Distributing to its shareholders will be received by a shareholder as a creditor, employee or in any capacity other than that of a shareholder of Distributing.
- (b) The five years of financial information submitted on behalf of Business 1 and Business 2 is representative of the present operations of Business 1 and Business 2, and, with regard to such businesses, there have been no substantial operational changes since the date of the last financial statements submitted.
- (c) Following the transaction, Distributing and Controlled will each continue the active conduct of its business, independently and with its separate employees, except for services to be provided by Distributing to Controlled, or vice versa, for a transitional period following the Distribution pursuant to the Separation Agreements.
- (d) The Distribution is carried out for the corporate business purpose of reducing conflict between the franchisees of Distributing and the franchisees of Controlled and eliminating conflict between the managements of Distributing and Controlled, which will improve the business prospects of both brands. The Distribution is motivated, in whole or substantial part, by one or more of these corporate business purposes.
- (e) The Distribution will not be used principally as a device for the distribution of the earnings and profits of Distributing or Controlled or both.
- (f) The Distributing Purchase Rights and the Controlled Purchase Rights are each of the type described in Rev. Rul. 90-11.
- (g) Distributing neither accumulated its receivables nor made extraordinary payment of its payables in anticipation of the transaction.

(h) No intercorporate debt will exist between Distributing and Controlled at the time of, or subsequent to, the Distribution, except that Distributing (or its successors) may owe Controlled, or Controlled may owe Distributing (or its successors) amounts payable under the Separation Agreements or in the ordinary course of business. Any such indebtedness owed by Controlled to Distributing upon completion of the Distribution will not constitute stock or securities.

(i) Immediately before the Distribution, items of income, gain, loss, deduction, and credit will be taken into account as required by the applicable intercompany transaction regulations (see §§ 1.1502-13 and 1.1502-14 as in effect before the publication of T.D. 8597, 1995-32 I.R.B. 6, and as currently in effect; § 1.1502-13, as published by T.D. 8597). Furthermore, Distributing's excess loss account, if any, with respect to Controlled Common Stock (or the excess loss account that Distributing may have in the stock of another member that is required to be taken into account by § 1.1502-19) will be included in income immediately before the distribution (see § 1.1502-19).

(j) Payments made in connection with all continuing transactions, if any, between Distributing and Controlled will be based on terms and conditions arrived at by the parties bargaining at arms' length.

(k) No two parties to the transaction are investment companies as defined in § 368(a)(2)(F)(iii) and (iv).

(l) The Distribution is not part of a plan or series of related transactions (within the meaning of §1.355-7) pursuant to which one or more persons will acquire directly or indirectly stock representing a fifty percent or greater interest (within the meaning of § 355(d)(4)) in Distributing or Controlled (including any predecessor or successor of any such corporation).

(m) To the best knowledge of the management of Distributing, there is no plan or intention on the part of any particular shareholder of Distributing to sell, exchange, transfer by gift or otherwise dispose of any stock in, or securities of, either Distributing or Controlled after the Distribution other than (i) ordinary market trading (ii) donations, sales or other dispositions by employees, officers and directors of Distributing or Controlled of shares of Distributing or Controlled (including shares obtained upon the exercise of stock options) for personal tax planning or personal financial planning reasons, and (iii) sales by Institutional Investors described hereinafter. To the best knowledge of the management of Distributing, no Institutional Investor (other than Shareholder D) has any plan or intention to sell,

exchange, transfer by gift, or otherwise dispose of any stock in Distributing or Controlled after the Distribution. Notwithstanding the forgoing, any Institutional Investor may in the future determine to dispose of or purchase stock of Distributing or Controlled in the normal course of its business based upon market conditions and investment needs in existence at that time.

(n) There is no plan or intention by Controlled, directly or through any subsidiary corporation, to purchase any of its outstanding stock after the transaction, other than the through the Controlled Repurchases.

(o) Distributing will not make any block purchases of shares after the transaction from any of the Institutional Shareholders nor will it make any block purchases from any other shareholder who owns five percent or more of the stock in, or the securities of, Distributing at the time of the purchase.

(p) The payment of cash in lieu of fractional shares of Controlled Common Stock is solely for the purpose of avoiding the expense and inconvenience to Controlled of issuing fractional shares and does not represent separately bargained for consideration. The total cash that will be paid in the Distribution to shareholders in lieu of fractional shares of Controlled Common Stock will not exceed one percent of the total consideration that will be distributed in the Distribution. The fractional share interests of each Distributing shareholder will be aggregated, and no Distributing shareholder will receive cash in an amount equal to or greater than the value of one full share of Controlled Common Stock.

## RULINGS

Based solely on the information submitted and the representations set forth above, we rule as follows:

1. No gain or loss will be recognized by Distributing on the Distribution. Section 355(c).
2. No gain or loss will be recognized by (and no amount will otherwise be included in the income of) the shareholders of Distributing Common Stock on the receipt of the Controlled Common Stock from Distributing. Section 355(a)(1).
3. The aggregate basis of the Distributing Common Stock and the Controlled Common Stock (including fractional interests that will be sold on behalf of such shareholders) in the hands of Distributing shareholders immediately after the Distribution will be the same as the

aggregate basis of the Distributing Common Stock held by such shareholders immediately prior to the Distribution, allocated in proportion to the fair market value of each in accordance with §1.358-2(a)(2). Sections 358(a)(1), (b), and (c).

4. The holding period of the Controlled Common Stock (including fractional interests) received by Distributing shareholders will include the holding period of the Distributing Common Stock with respect to which the Distribution was made, provided that such Distributing Common Stock is held as a capital asset on the date of the Distribution. Section 1223(1).
5. Any payment of cash in lieu of fractional shares of Controlled Common Stock will be treated for federal income tax purposes as if the fractional shares were issued in the Distribution and then were redeemed by Controlled. The cash payments will be treated as having been received as a distribution in full payment in exchange for the shares redeemed as provided in section 302(a). Provided the fractional share interest is a capital asset in the hands of the recipient shareholder, the gain or loss will constitute capital gain or loss subject to the provisions and limitations of Subchapter P of Chapter 1. Rev. Rul. 66-365, 1966-2 C.B. 116; Rev. Proc. 77-41, 1977 2 C. B. 574.
6. Earnings and profits will be allocated between Distributing and Controlled in accordance with §§ 312(h), 1.312-10(a) and 1.1502-33(e)(3).
7. Controlled's distribution of the Controlled Note to Distributing and the in-kind distribution by Controlled of the d of net notes and accounts receivable to Distributing will be treated for federal income tax purposes as an intercompany distribution to which §§ 301 and § 1.1502-13(f)(2) apply.
8. Payments made by Distributing to Controlled or by Controlled to Distributing under the Separation Agreements that (i) have arisen or will arise for a taxable period ending on or before the Distribution or for a taxable period beginning before and ending after the Distribution and (ii) will not become fixed and ascertainable until after the Distribution, will be treated as occurring immediately before the Distribution. See *Arrowsmith v. Commissioner*, 344 U.S. 6, 73 S. Ct. 71, 97 L. Ed. 6, 1952-2 C.B. 136 (1952); Rev. Rul. 83-73, 1983-1 C.B. 84.

## CAVEATS

No opinion is expressed about the tax treatment of the Distribution under other provisions of the Code or regulations or the tax treatment of any conditions existing at the time of, or effects resulting from, the Distribution that are not specifically covered by the above rulings. In particular, no opinion is expressed regarding whether the proposed transaction: (i) satisfies the business purpose requirement of § 1.355-2(b); (ii) is used principally as a device for the distribution of the earnings and profits of the distributing corporation or the controlled corporation or both (see §§ 355(a)(1)(B) and 1.355-2(d)) or (iii) is part of a plan (or series of related transactions) pursuant to which one or more persons will acquire directly or indirectly stock representing a fifty percent or greater interest in the distributing corporation or the controlled corporation under § 355(e)(2)(A)(ii).

## PROCEDURAL STATEMENTS

This ruling is directed only to the taxpayer that requested it. Section 6110(k)(3) provides that it may not be used or cited as precedent. A copy of this letter must be attached to any income tax return to which it is relevant. Alternatively, instead of attaching a copy of this letter to the returns, taxpayers filing their returns electronically may attach a statement to the return that provides the date and control number of the letter ruling.

In accordance with the power of attorney on file in this office, a copy of this ruling letter will be forwarded to your authorized representative.

Sincerely,

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Michael J. Wilder  
Senior Technician Reviewer, Branch 1  
Office of Associate Chief Counsel (Corporate)